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In the

Supreme Court of the United States

OCTOBER TERM 1965

No. 1100

SOUTHWESTERN LIFE INSURANCE COMPANY
AND VALLEY ROYALTY CORPORATION,
Petitioners,

v.

PAN AMERICAN PETROLEUM CORPORATION
AND SOCONY MOBIL OIL COMPANY, INC.,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

JAMES P. SWIFT,
P. O. Box 2699,
Dallas, Texas 75221,
Counsel for Petitioners.

WARLICK PRESS, INC.—2203 VALDINA STREET—DALLAS—ME 1-3130

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Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

Petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above-entitled case December 30, 1964.

CITATION TO OPINION BELOW

The opinion of the Court of Appeals, printed in Appendix A hereto, infra, p. 1, is reported in 340 F. 2d 211.

JURISDICTION

The judgment of the Court of Appeals were entered on December 30, 1964, R. p. 288; p. A-33, infra. Rehearing was denied on March 3, 1965, R. p. 352; p. A-35, infra. The juris-

diction of this Court is invoked under 28 U.S.C.A., Sec. 1254(1).

QUESTIONS PRESENTED

1.

If the mortgagor of an oil lease steals oil from an adjoining lease not covered by the mortgage and delivers it to a pipeline purchaser, representing it to be the product of his own lease, and directs the pipeline purchaser to pay to the mortgagee the proceeds of the sale and the purchaser pays monies to the mortgagee representing them to be the sale proceeds of oil produced from the mortgaged lease, is the mortgagee liable to the person from whom the oil was stolen notwithstanding the money was received by the mortgagee in good faith, in the regular course of business and without notice of the theft?

2.

Whether the execution of a division order by an innocent mortgage holder, together with the lease owner-producer, whereby the purchaser of oil produced from a leasehold specifically described in the division order is directed to pay to the mortgage holder the proceeds of such sale renders the mortgage holder liable for the value of oil stolen by the producer from an adjoining lease owner and delivered by the producer to the purchaser as oil produced from the mortgaged leasehold?

3.

Whether the right reserved to a mortgage holder to take possession of and operate an oil lease in certain events, where

such right was never exercised, makes the mortgage holder liable for the acts of the mortgagor-operator of the lease in stealing and disposing of the oil of an adjoining lease owner, notwithstanding the mortgage holder's innocence of any complicity, it appearing that the purchaser of the oil paid to the mortgage holder monies equivalent to the sale price of the oil.

4.

Whether an innocent mortgage holder, receiving from the pipeline purchaser monies equivalent to the sale price of oil purchased from the mortgagor-lease owner, if liable to the person from whom the mortgagor-lease owner stole the oil for that portion of the monies received and applied to the debt, is also liable to the person from whom the oil was stolen for the portion of such monies paid over to the mortgagor-lease owner pursuant to the requirements of the mortgage.

STATEMENT

Respondents, Delaware and New York corporations, respectively, sued one H. L. Long, citizen of Texas, owner and operator of an oil and gas lease known as the Long-Willie-Starr lease (herein called the Long lease), in East Texas, and other persons, citizens of Texas and Georgia, who were co-owners of the lease and also these Petitioners, Texas corporations, asserting that oil of a value exceeding $620,000, ostensibly produced and sold from the lease to a pipeline purchaser, was in fact stolen by means of deviated wells from

adjoining leaseholds owned by Respondents. (R. 43-44, 47.) The pipeline purchaser was not sued. Valley Royalty Corporation is the subsidiary of Southwestern Life Insurance Company and the term "SwL" has been used by the lower court to refer to both as a single entity. Appendix A, infra, p. 3, footnote 3. We use "Petitioners" in the same sense. Petitioners owned notes secured by mortgages (deeds of trust) on the interests of the various lease owner-defendants and also owned production payments (limited overriding royalties) payable out of the oil and gas produced from the Long lease and out of the proceeds of the sale of such oil and gas. Plaintiffs Exhibits 1D and 3 are typical. As found by the court below the mortgages and production payments are to be treated alike because they have identical consequences in this case. Appendix A, infra, p. 18, footnote 29. Petitioners had no knowledge prior to the filing of the suit that oil was being stolen from Respondents. (R. 132, Appendix A, infra, p. 16, footnote 27). Petitioners never had possession or control of the Long lease nor of any oil produced from that or any other lease. (R. 222.) By the terms of the mortgages and production payments and certain division orders, prepared by the pipeline purchasers and executed by the lease owners and Petitioners, the pipeline purchasers were directed to pay to Petitioners the sale proceeds of oil and gas produced by and purchased from the Long lease. (Plaintiffs Exhibits 3-1 and 6-C are typical). The mortgages and production payments authorized Petitioners to apply specified portions of these monies received from the pipeline purchasers toward liquidation of these obligations and required Petitioners to pay over the surplus

to the lease owners. (R. 194-196, Appendix A, infra, pp. 6-8, footnotes 8, 9 and 10.) The mortgages and production payments contain provisions whereby the lease owners are obligated to operate the lease in compliance with all applicable laws, rules, and regulations, to pay all taxes levied thereon (Appendix A, infra, p. 5, footnote 6) and whereby Petitioners were given rights of inspection of the property, the right to perform covenants in default by the lease owners, and in the event of certain defaults to take possession of and operate the property until the obligations are paid. (Appendix A, infra, p. 6, footnote 7). None of these rights was ever exercised. (R. 222, Appendix A, infra, pp. 20, 31).

The pipeline purchasers paid to Petitioners sums equal to the purchase price of all oil delivered to them by the operator, Long. Respondents were awarded judgment in the trial court against the lease owner-defendants in sums totaling over $800,000 and they did not appeal; against Petitioners for all sums received by Petitioners during the period of two years preceding suit (with interest $232,145.42), the trial court holding the Texas 2-Year Statute of Limitations barred recovery for monies received earlier, but the court allowed no deduction for the surplus monies paid over by Petitioners to the lease owners. (Appendix A, infra, p. 2). This judgment was affirmed by the Court of Appeals, Judge Garza dissenting to the part which allowed no deduction for the sums paid over by Petitioners to the lease owners ($100,085.18). (Appendix A, infra, pp. 30-32). The judgment below is based solely on the holding that by reason of the rights reserved to them by

the mortgages and production payments Petitioners were guilty of conversion of Respondents' oil.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is in conflict with the rule announced by this Court in *Holly v. Domestic and Foreign Missionary Society*, 180 U.S. 284, 21 Sup. Ct. 395, 45 L.Ed. 531 (1901), in which this Court held that a creditor who in good faith in the regular course of business receives money in payment of a debt is not subject to the risk of accounting therefor to a third person who may be able to show that the debtor obtained it from him by felony or fraud. The decision is also in conflict with the principles announced by this Court in *Fidelity Mutual Life Ins. Co. v. Clark*, 203 U.S. 64, 27 Sup. Ct. 19, 51 L.Ed. 91 (1906), holding that even the strongest claim of the true owner of money will not prevail against an innocent recipient who unwittingly actually participated in the fraud whereby the money was taken from the true owner. In the case at bar there is no intimation that Petitioners were even remotely involved in any fraudulent transaction. They were innocent victims of the same illicit scheme executed against Respondents.

2. The court below arrived at its decision primarily on the theory that the powers given in Petitioners' security instruments, though unexercised, constituted sufficient exercise of dominion and control over Respondents' property as to amount to a conversion thereof. (Appendix A, infra, p. 18). This holding is contrary to the settled law of Texas on a

question of far reaching importance. It is a matter of common knowledge that the oil industry is vital to the economy of Texas as well as that of the entire nation and that the financing of transactions in that industry, as in all industries, is essential to its health.

The effect of the decision of the lower court is to make a mere mortgage holder liable for the torts of his debtor, the mortgagor. No judicial precedent is cited by the court for this conclusion and none is believed to exist. On the contrary the courts of Texas have uniformly held otherwise. *Snodgrass v. Kelley*, 141 S.W. 2d 381, Tex. Civ. App., (1940) writ ref.; *American Cotton Co-Op v. Plainview Compress & Warehouse Co.*, 114 S.W. 2d 689, Tex. Civ. App., (1938) writ dism.; *John Hancock Mut. Life Ins. Co. v. Howard*, 85 S.W. 2d 986, Tex. Civ. App., (1935) writ ref.; *De La Moriniere v. Sam*, 8 S.W. 2d 312, Tex. Civ. App., (1928); and *Ashbrook v. Hammer*, 106 S.W. 2d 776, Tex. Civ. App., (1937). Moreover they have adhered to the rule that conversion is the unlawful and wrongful exercise of dominion, ownership, or control by one person over the property of another, to the exclusion of the exercise of the same rights by the owner. *France v. Gibson*, 101 S.W. 536, Tex. Civ. App., (1907); *Compton v. Farrington*, 16 S.W. 2d 345, Tex. Civ. App., (1929); *Sunray Enterprises v. Rosenaur*, 335 S.W. 2d 670, Tex. Civ. App., (1960, writ ref., N.R.E.: *Cantrell v. Broadnax*, 306 S.W. 2d 429, Tex. Civ. App., (1957), and cases cited 14 Tex. Jur. 2d 5, Sec. 1 of Conversion. This rule is quoted with approval in the opinion of the lower court (Appendix A, infra, p. 14) but nowhere in its opinion nor in the record

is there any single reference to or evidence of any exercise of dominion or control over Respondents' property except such as is said by the lower court to be contained in the security instruments held by Petitioners and in the division orders executed by Petitioners, along with the lease owners. All of these instruments refer exclusively and by specific description to the Long lease. None makes any reference whatsoever to Respondents' leasehold, Respondents' oil, or any other property of Respondents. It is therefore beyond dispute that if any link exists between Petitioners and the property of Respondents it must be found in the fact that Petitioners received from the pipeline purchasers of the oil stolen by Long from Respondents money purporting to be the equivalent of the purchase price of oil produced by the Long lease. But this money was not the money of Respondents. It was the money of the pipeline purchasers in the form of checks on their own bank accounts. (R. 247). It follows that the case must fall within the rule of *Holly v. Domestic and Foreign Missionary Society*, 180 U.S. 284, 21 Sup. Ct. 295, 45 L.Ed. 531 (1901). The rule of *Holly* has been applied by the Texas courts many times. *Texas State Bank of Walnut Springs v. First National Bank of Meridian*, 168 S.W. 504, Tex. Civ. App., (1914); *American Surety Company v. Bache*, 82 S.W. 2d 181, Tex. Civ. App., (1935) writ ref.; *W. Horace Williams Company v. Vandaveer*, 84 S.W. 2d 333, Tex. Civ. App., (1935) writ. dism.; *Burnett's Trust v. Farmers State Bank in Mexia*, 175 S.W. 2d 453, Tex. Civ. App., (1943) writ ref.; *Sinclair Houston Federal Credit Union v. Hendrick*, 268 S.W. 2d 290, Tex. Civ. App., (1954) writ. dism.

It has often been applied in other jurisdictions. *Kean v. National City Bank*, 294 F. 214 (Sixth Circuit); *Walker v. First National Bank of Athena*, 72 p. 635, 45 Ore. 102; *Gaffner v. American Financing Company* (Wash 1922) 28 A.L.R. 624, 206 p. 916; *Nye v. Johnson*, 4 N.W. 2d 819, 72 N. Dak. 95 (1942); *Leonard v. Tidd*, 3 Metc. (44 Mass.) 6; *Stephens v. Board of Education of City of Brooklyn*, 79 N.Y. 183, 35 Am. Rep. 511; *Leuthold v. Fairchild*, 35 Minn. 99, 27 N.W. 503, 28 N.W. 218. Nor may these cases be distinguished on the ground that the payments received by Petitioners were not made by the person who actually stole and sold the oil but by the purchaser thereof. Here the pipeline purchasers were acting on the express directions of the culprit and his co-owners of the Long lease and the payment by the purchasers produced the identical consequences as if the lease owners had collected the sales proceeds and paid them over to Petitioners or paid them to a bank with directions to pay them to Petitioners, *White v. Miners' National Bank*, 102 U.S. 658, 26 L.Ed. 250; *West v. Rule*, 195 S.W. 230; Tex. Civ. App., (1917).

The lower court dismisses the objection that the documentation, on which it rests its finding of a conversion of Respondents' property, makes no mention of any property of Respondents with the remark that this argument is based on a technical, literal reading of the instruments, (Appendix A, infra, p. 24). It is strange logic that the documents, which by themselves are said to form the whole foundation of liability, can be so construed as to confer control over property

to which they do not even remotely refer. In the words of Justice Whittaker (retired):

> "I believe we ought to be able to agree that words—though not ends in themselves—are our only tools and means of communicating thoughts and ideas. Hence, plain and unambiguous words surely should be taken and adhered to in their commonly accepted sense, for otherwise the result must necessarily be the loss of all means of communicating with certainty; and all documents, however carefully prepared, would become mere 'scraps of paper'. This, carried to an illustrative extreme, would even make it dangerous for a borrowerer to sign, or for a lender to accept, a simple promissory note." *American Bar Journal*, January 1965 (Vol. 51, P. 28).

To the same effect is the holding of the Fifth Circuit in *Fowler v. Pennsylvania Tire Co.*, 326 F. 2d 526 (1964). Courts are not at liberty to revise agreements while professing to construe them. *J. R. Gray Co. v. Jacobs*, 362 S.W. 2d 167, Tex. Civ. App. (1962), writ ref., N.R.E.

Conversion is a tort growing out of the unlawful exercise of control over the possession, not merely the title, to personal property. In order to constitute a conversion there must be an unlawful interference with the possession of the property, *John Hancock Mutual Life Ins. Co. v. Howard*, 85 S.W. 986, Tex. Civ. App. (1935), writ ref., which also illustrates the rule that mere words and declarations will not amount to a conversion. To the same effect is *American Cotton Co-Op Association v. Plainview Compress and Warehouse Company*, 114 S.W. 2d 689, Tex. Civ. App. (1938), writ dism., holding in an analogous fact situation that to establish conversion the person charged must have unlaw-

fully and wrongfully exercised dominion and control over the property.

The lower court has held the lender responsible for the wrongful and illegal acts of a mere borrower in the total absence of a tortious act by the lender and in the total absence of any exercise by the lender of control over acts of the borrower. If the rule thus declared is to become the law no lender can advance its money under the usual form of mortgage (Williams & Meyers Oil and Gas Law, Sec. 428.8, Vol. 2, and 6 Stayton Texas Forms p. 685, Sec. 3703, illustrate that there was nothing novel or unusual about the form of the security papers) without being exposed to liability for wrongful acts of which the lender has no knowledge, in which it did not participate and for which under no other rule of law could it have liability. Such a rule is a new departure from the settled law of the land and is of such far reaching consequences as to justify exercise of the corrective power of this Court.

3. Petitioners were bound by the terms of the same security documents on which, alone, the lower court bases its judgment, to pay over to the lease owners certain proportions of the monies paid to Petitioners by the pipeline purchasers. Petitioners' obligation to pay over to the lease owners all monies in excess of the specified portions applicable to their investments was absolute (R. 194-196). Notwithstanding the absence of any right in Petitioners to keep or appropriate the money, the lower court has held them liable to Respondents therefor. It was stipulated that the monies so paid over amounted to $100,085.18. (R. 76-77, 194-196). The

majority opinion of the lower court cites no precedent for its holding, which directly conflicts with the principle announced by the same court in *Gulf Oil Corp. v. Lone Star Producing Co.*, 322 F. 2d 28 (1963), relied on in the dissenting opinion. In that case the Fifth Circuit held that Lone Star, as payee of certain overpayments which it had in turn disbursed to royalty owners and for production taxes, was liable only to the extent it benefited from the erroneous overpayments.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

JAMES P. SWIFT,
P. O. Box 2699,
Dallas, Texas 75221,
Counsel for Petitioners.